

Under Illinois law, "true leases" and "leases" that are actually conditional sales contracts are treated differently for Retailers' Occupation and Use Tax purposes. See 86 Ill. Adm. Code 130.2010. (This is a GIL).

May 15, 2001

Dear Xxxxx:

This letter is in response to your letter dated April 16, 2001 to Director Glen Bower. Director Bower has requested that I respond to your letter. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be accessed at the Department's Website at <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

In your letter, you have stated and made inquiry as follows:

Please find a copy of an invoice from AAA, a subsidiary of BBB. In the areas marked on the invoice you will notice that the invoice date is 2/15/01 and the payment due date is 2/01 01. The production of the invoice, 15 days after the payment due date makes it impossible to pay the bill on time, therefore automatically resulting in a late fee of \$10.00.

Additionally, on the invoice you will notice an item labeled Sales Tax in the amount of 0.52. The Pennsylvania sales tax rate is 6% and the Illinois sales tax rate is 6.25%. The rate on the invoice calculates to 1.44%. Upon questioning the sales tax with the company, in a letter dated 2/27/01, copy attached, the company does not identify the state for which they are collecting the sales tax. Additionally, the company states that the '...tax monies received are forwarded to the county in which the merchant resides'. State sales taxes are levied and collected by the states, not counties. It is clear that the company is in violation of PA or IL state revenue regulations.

I have corresponded with the company since December 30, 2000 attempting to have them properly explain and correct their billings, assuming the items in question are errors. To date, the company has refused to comply. Recently, I escalated the complaints to PERSON OF BBB. Shortly after that correspondence, the company ceased the billing and initiated an accelerated demand on the lease, requiring immediate full payment of the balance of the lease. I am not sure if this was coincidental or if the billing was stopped to prevent an on going paper trail of improper or possibly illegal billings.

In my opinion, that the company has established improper or illegal billing practices which force a late fee to be imposed on a monthly basis and refused to stop this practice. Additionally, the collection of sales taxes at a rate other than the billing or receiving state and implying that the taxes are paid to a county level Vs. the proper state

implies that the monies collected as sales tax may not be legal and/or may not be submitted to any state.

I am not sure if the company's actions have been intentional fraud to collect additional money to which they are not entitled or if the company's business practices are out of control. However, after bringing this to the attention of a Senior Vice President with no adequate response makes me feel that there may be intent to defraud.

Please investigate this matter as there may be many other people being subjected to this company's questionable activities.

Your letter contains statements and questions about a particular lease. Please be advised that Illinois sales tax liabilities associated with leases depend upon the specific terms of a lease. We are unable to provide more specific information without first reviewing a copy of the lease. We hope the following general information about leasing is helpful, however.

We have enclosed a copy of 86 Ill. Adm. Code 130.2010, the Department's regulation that covers the taxation of leases. Although your questions presume that rental receipts are subject to sales tax, that is generally not true in Illinois for rental payments received pursuant to true leases. Under Illinois law, "true leases" and "leases" that are actually conditional sales contracts are treated differently for Retailers' Occupation and Use Tax purposes. Lessors incur Use Tax liability on their cost price of tangible personal property that they acquire to use by leasing under true leases in Illinois. This means lessors in Illinois encounter a front-end tax on value rather than an amortized tax on receipts. The only exception is automobiles rented for one year or less, which are subject to the Automobile Renting and Use Tax found at 35 ILCS 155/1 et seq.

True leases generally have no buy out provisions at the close of the leases. If buy out provisions do exist, they must be fair market value buy out options in order to maintain the character of the true leases. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See, 86 Ill. Adm. Code 130.220(a). As end users of tangible personal property located in Illinois, lessors incur Use Tax liability on their cost price of such property. Except for short-term automobile rentals, there is no tax due upon rental receipts in Illinois.

In other words, lessees incur no tax liability under true leases. Lessors, instead, are the parties that incur tax liability. Lessors in these circumstances have no legal authority to collect "tax" from lessees. If such lessors collect "tax" from lessees, they are making an overcollection of tax. When sellers make overcollections, purchasers have a legal right to claim a refund of such amounts from the sellers. If refunds are not made, sellers are legally required to pay the tax to the Illinois Department of Revenue. See, 35 ILCS 120/2-40. Many times, lessors and lessees under true leases enter into contractual agreements providing that lessees will reimburse lessors for the tax liability incurred by the lessors. If such contracts have been made, the lessees are obligated to fulfill the terms of the contracts.

Under Section 130.2010(a), persons who purport to "lease" the use of property, but in fact sell such tangible personal property to nominal "lessees," are considered to be making conditional sales subject to Retailers' Occupation Tax. Such would be the case when the agreements contain nominal purchase options at the end of the lease term. In these situations Retailers' Occupation Tax is due on all the payments received by the "lessors." Interest or finance charges are excluded from gross receipts. In the absence of adequate records showing what such charges actually are, the

Department will presume that such charges are not in excess of like charges which are customarily made in the trade. See 86 Ill. Adm. Code 130.420, enclosed.

Assuming that your lease is a true lease, we do not believe that you will incur any Illinois State tax liability. As noted above, there is no tax on rental receipts. Rather, the lessor incurs an Illinois Use Tax liability "up front" on the cost price of the tangible personal property purchased for leasing purposes. We note that the invoice attached to your letter contained a line item for "sales tax." If you have entered into a true lease, as explained above, the lessor appears to have made an overcollection of tax. He must either refund this "tax" to you or remit it to the Department.

While we believe you will not incur any Illinois State tax on your rental receipts, we cannot rule on the application of any local taxes which are not administered by the Department. The City of Chicago, for instance, imposes and administers a Transaction Tax. Since the Department of Revenue does not administer or collect this tax, you may wish to contact the City of Chicago directly for more information.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Karl W. Betz
Associate Counsel

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Enc.